IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-1791

ARTHUR ANDERSEN & Co.,

Petitioner,

—v.—

MITCHELL A. KRAMER and DAVID C. HARRISON,

Respondents.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

DONALD N. RUBY
845 Third Avenue
New York, New York 10022

Attorney for Respondents

Of Counsel:

LESTER L. LEVY
WOLF POPPER ROSS WOLF & JONES
845 Third Avenue
New York, New York 10022

MEILEN PRESS INC. — N. Y. C. 219

INDEX

TABLE OF AUTHORITIES

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This brief is submitted in opposition to the petition for writ of certiorari of Arthur Andersen & Co., one of the defendants herein, which seeks review of a judgment and decision of the United States Court of Appeals for the Third Circuit, entered in these proceedings on April 20, 1976.

That decision dismissed the appeal of petitioner, taken pursuant to 28 U.S.C. § 1291,[1] from an interlocutory class action certification order entered by the United States District Court for the Eastern District of Pennsylvania. Dismissal of the appeal was required by the final judgment rule applied in accordance with well settled principles established by this Court and consistently followed by all

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[1] 28 U.S.C. § 1291 is set forth at Appendix A-1.

the Circuit Courts. This Court has declined to review such principles on many recent occasions. *Touche Ross & Co.* v. *Seiffer,* 96 S.Ct. 779 (1976); *Cessna Aircraft Co.* v. *White,* 96 S.Ct. 363 (1975); *Touche Ross & Co.* v. *Fabrikant,* 96 S.Ct. 424 (1975); *Hackett* v. *General Host Corp.,* 407 U.S. 925 (1972).

The interlocutory class action certification order appealed from in this suit does not differ from the orders appealed from in the aforesaid actions. Aware of this, petitioner seeks to have the interlocutory determination of class certification reviewed by this Court by recklessly charging respondents with "unethical behavior", "strike suits", "deceit", "professional impropriety", et al. These charges have been repeatedly made in this action by petitioner to the District Court and to the Court of Appeals for the Third Circuit. In marked contrast to petitioner's vitriolic attacks on respondents, the District Court has determined that the complaint sets forth valid claims for relief against defendants, including petitioner, for violation of the federal securities laws, that the case was properly brought as a class action, and that respondents will fairly and adequately protect the interests of the class, and the Court of Appeals has remarked that respondents have demonstrated an awareness of fealty to the Code of Professional Responsibility. Petitioner is now attempting to have this Court make a factual determination to the contrary (i.e., that respondents are unethical), in order to reverse the trial judge's exercise of discretion under Fed. R. Civ. P. 23 in certifying this action as a class action.

Questions Presented

Does an appeal lie under 28 U.S.C. §1291 challenging the propriety of a trial judge's exercise of discretion in issuing

an interlocutory order which determined that the requirements of F.R.C.P. Rule 23[2] had been met?

Should this Court review the factual determinations of the District Court and the Court of Appeals for the Third Circuit which did not sustain petitioner's charges of strike suit, deceit, unethical conduct and the like?

Statement of the Case

Respondents, on January 6, 1969, purchased, as joint tenants, common stock of Scientific Control Corp. ("Scientific"), in reliance on a prospectus, as well as upon financial reports and other data of Scientific regarding the coporation's financial condition, which, they allege, deceived them and other purchasers as to the true worth of the stock. Less than thirteen months after the effective date of registration and original offering of the stock, Scientific filed a petition for an arrangement under Chapter XI of the Bankruptcy Act.

Respondents filed their complaint on August 9, 1971, for damages pursuant to Sections 11, 12(2), 15 and 17(a) of the Securities Act of 1933 (15 U.S.C. § 77 k, 77 l(2), 77 o and 77 q(a), and Sections 9(a)(4), 10(b) and 18 of the Securities Exchange Act of 1934, 15 U.S.C. § 78 i(a)(4), 78 j(b) and 78 r, the rules and regulations thereunder and common law fraud principles.

The prospectus and the other financial reports on Scientific failed to reveal, among other items, a liability of $500,000 incurred by Scientific before the date of the prospectus and the fact that all accounts receivable had been pledged as collateral for obligations incurred by

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[2] The relevant provisions of F.R.C.P. Rule 23 are set forth in Appendix A-1, 2, 3.

Scientific. The District Court has noted that the inclusion of the amount of the $500,000 loan in the Registration Statement would have increased Scientific's current liabilities by almost 50%. [365 F.Supp. at 789, note 10.]

The defendants are Scientific; H.L. Federman & Co., and Kleiner, Bell & Co., Inc., the principal underwriters of the issuance of 400,000 shares of Scientific common stock; petitioner, the accountant for Scientific; and the individual defendants, who were officers and/or directors of Scientific.

Prior Proceedings In This Action

Fourteen of the defendants (including petitioner) filed motions to dismiss the complaint on various grounds or to quash service of process. In its decision of September 27, 1973, as amended November 27, 1973, the District Court determined that respondents had stated valid claims for relief against petitioner and other defendants under the Securities Act of 1933 and the Securities Exchange Act of 1934.[3]

On October 1, 1974, the District Court determined that the case may proceed as a class action on behalf of all persons, except defendants, who purchased stock of Scientific pursuant to or in reliance on the prospectus and the other reports regarding the corporation's financial condition from October 31, 1968 to November 21, 1969.[4] Defendants did not dispute that the purchasers of the stock

[3] This decision is reported at 365 F.Supp. 780. The District Court dismissed the claims brought under §9(a)(4), 15 U.S.C. §78i(a)(4), and granted the motions of defendants Kleiner, Bell & Co., Inc. and H.L. Federman & Co. to dismiss the claims brought against them under Sections 12(2), 15 and 17(a)(2) of the Securities Act of 1933.

[4] This decision is reported at 64 F.R.D. 558 (1974).

during that period were too numerous to be joined conveniently in the action. They, rather, opposed respondents' motion for a class determination by impugning the motives of respondents (the class representatives).

The Court stated that defendants' attack on the size of respondents' individual claims is not dispositive of whether they will adequately represent the class and noted that: "From our observation of the manner in which plaintiffs have proceeded with this action up to this juncture, we conclude that they will fairly and adequately protect the interests of the class." 64 F.R.D. at 559. And, in a statement that we submit is dispositive of this petition for writ of certiorari challenging the class action determination, the District Court stated that its decision to allow the case to proceed as a class action did not mean that defendants' opportunity to seek to deny class action determination had been *finally* determined. 64 F.R.D. at 559.

On April 17, 1975, the District Court denied petitioners' motion for reconsideration of its class action certification or, in the alternative, for a certification pursuant to 28 U.S.C. § 1292 (b).[5] Petitioner appealed this decision under 28 U.S.C. § 1291.

On June 20, 1975, petitioner moved the District Court, *inter alia*, to disqualify respondents' counsel, alleging that there was an irreconcilable conflict of interest between respondents' representation by the law firm of Kramer & Salus and the representation of the members of the class by the respondents. The District Court denied the motion and petitioner appealed.

The Court of Appeals decided both appeals together. It dismissed petitioners' appeal from the class certification

[5] This decision is reported at 67 F.R.D. 98 (1975).

decision, holding that such a determination was not an appealable final order under 28 U.S.C. § 1291. It determined, on the other hand, that the order denying the motion to disqualify respondents' counsel was appealable under the collateral order doctrine of *Cohen* v. *Beneficial Industrial Loan Corp.*, 337 U.S. 541 (1949). In its decision,[6] the Court of Appeals assumed that the professional representation rendered by respondents' attorneys was of the highest calibre, and that respondent Kramer had rightly limited his interest in these proceedings to that of a member of the class.[7] The Court of Appeals stated that respondent Kramer "acted wisely" in the position he articulated in his deposition that he would not accept any portion of a court-awarded attorneys' fee derived from this case because he perceived that he could be accused of conflict of interest were he to benefit from the case other than as a member of the class.[8] The Court of Appeals also noted that respondent Kramer "demonstrated an awareness of fealty to the spirit of Canon 9 of the Code of Professional Responsibility.[9] It went on to say that although respondents have stated: that they will receive no portion of any attorneys' fee that is awarded in this case; that no close association exists between respondent Harrison and the counsel to the class, as they have never been professionally associated; and both respondents, although attorneys, have stated that their role in this litigation is limited to that of a party-plaintiff—these facts while they may effectively guard against an accusation of professional impropriety, do not meet the criticism that the retention of attorneys

[6] This decision is set forth in Appendix A to the Petition For Writ of Certiorari.

[7] Id. at p. A-8.

[8] Id. at p. A-9.

[9] Id. at p. A-10.

associated with respondent Kramer contravened the appearance of propriety. "And it is the *appearance,* not the *fact* of impropriety which Canon 9 is designed to eliminate." [10]

The Court, commenting that Ethical Consideration 9-2 of the Code of Professional Responsibility cautions that . . . "on occasion, ethical conduct of a lawyer may appear to laymen to be unethical",[11] concluded that the vindication of the Code of Professional Responsibility with respect to the appearance of impropriety required it to grant the request for disqualification of Steven Kapustin as counsel for the class. It ruled that disqualification of Kapustin would not work an undue hardship on the class, since the issue of liability is not complex and should not consume too much trial time, thus new counsel should not require an inordinate amount of time to become sufficiently familiar with the case to proceed to trial.

By reason of the decision of the Court of Appeals, respondents have retained new counsel for the class in place of Steven Kapustin to prosecute this action.[12]

Petitioner filed a petition for writ of certiorari with respect to that portion of the Court of Appeals decision which held that the interlocutory class certification herein was not a final order under 28 U.S.C. § 1291.

[10] Id. at p. A-13.

[11] Id. at p. A-13.

[12] Respondents have retained the law firm of Wolf Popper Ross Wolf & Jones, whose expertise and competence in this field has been judicially noted on several occasions. See, for example, the comments of Judge Walter Mansfield in *Berland* v. *Mack*, 48 F.R.D. 121, 127, 128 (S.D.N.Y. 1969), (a suit wherein the Wolf Popper firm had been appointed lead counsel by Judge Mansfield).

Reasons for Denying the Writ

The sole issue before this Court is whether an appeal lies under 28 U.S.C. § 1291 challenging the propriety of a trial judge's exercise of discretion in issuing an interlocutory order which found that the requirements of F.R. Civ. P. 23 had been met. The petition for writ of certiorari should be denied because the interlocutory class order from which petitioner appealed under § 1291 was not a final order, and would not have been appealable as an exception to the final judgment rule in any Circuit. There is no difference of opinion among the Circuits on that question.

Petitioner, attempting to obfuscate the sole issue before the Court, has chosen to charge respondents with unethical conduct, deceit, professional impropriety, commencing a strike suit, etc. As a review of the previous decisions in this action evidences, those charges have not been sustained by the Court of Appeals or by the District Court. Petitioner's attempt to have this Court make a factual determination to the contrary in an attempt to deny the purchasers of Scientific common stock class representation represents a misuse of the petition for writ of certiorari procedure.

POINT I

The Instant Class Certification Order Is Not Appealable Under § 1291 As a Final Order.

It is axiomatic that the Courts of Appeals have jurisdiction over appeals of right under 28 U.S.C. § 1291 only from "final decisions" of the district courts. The statutory limitation is the product of a policy judgment about judicial administration which was written into the first Judiciary

Act and adhered to ever since. See, *Cobbledick* v. *United States*, 309 U.S. 323, 324-325 (1940). The requirement eliminates the waste of judicial time and the obstruction to just claims that would come from permitting a succession of separate appeals from the various rulings to which a litigation may give rise from its initiation to entry of judgment. *Cobbledick, supra,* at 325.

The final judgment rule is of such crucial importance to the efficient and just administration of the federal judicial system that this Court has recognized that a litigant should be permitted to depart from that rule only in an extremely narrow category of cases where the non-final order appealed (1) is separable from and collateral to the claims asserted in the action, (2) would finally determine the collateral question, and (3) would result in irreparable harm by any delay in appeal. *Cohen* v. *Beneficial Industrial Loan Corp.*, 337 U.S. 541 (1949).

The Courts of Appeals have been uniform in holding that interlocutory class action certification orders of the type at issue herein, do not fall within the *Cohen* doctrine. *In re Master Key Antitrust Litigation*, 528 F.2d 5 (2d Cir. 1975); *Blackie* v. *Barrack*, 524 F.2d 891 (9th Cir. 1975); *Hellerstein* v. *Mr. Steak, Inc.*, 531 F.2d 470 (10th Cir. 1976); *King* v. *Kansas City Southern Industries, Inc.*, 479 F.2d 1259 (7th Cir. 1973); *Hackett* v *General Host Corp.*, 455 F.2d 618 (3rd Cir.), *cert. denied*, 407 U.S. 925 (1972); *In re Cessna Aircraft Distributorship Antitrust Litigation*, 518 F.2d 213 (8th Cir. 1975); *Walsh* v. *City of Detroit*, 412 F.2d 226 (6th Cir. 1969).

These decisions recognize that under Rule 23, the district court is given broad discretion to determine the maintainability and the conduct of class actions. By the very language of the rule, any order rendered by the district court regarding the maintenance of the class action "may

be considered conditional, and may be altered or amended before any decision on the merits." Fed. R. Civ. P. 23 (c)(1). The District Court in this case specifically recognized the non-finality of its class action determination.

Given these facts, it is apparent that the order here cannot be considered "final" in the manner indicated by the *Cohen* and *Eisen IV*[13] decisions. *In re Cessna Air. Distrib. Antitrust Litigation,* 518 F.2d 213 (8th Cir. 1975), *cert. denied,* 96 S.Ct. 363; *Hellerstein* v. *Mr. Steak, Inc.,* 531 F.2d 470 (10th Cir. 1976).

Petitioner's theory that *Eisen IV* mandates the Courts of Appeals to review all interlocutory class certification orders if they are immediately appealed has been rejected time and again. See, *In re Cessna Air Distrib. Antitrust Litigation, supra; Hellerstein* v. *Mr. Steak, Inc., supra; Blackie* v. *Barrack, supra.* The district court's order in *Eisen IV* had directed that 90% of the cost of notice should be paid by the defendants and had dispensed with individual notice to members of the class whose identity was readily attainable. If defendants had paid for 90% of the costs of notice and the order directing payment was eventually found improper, it was evident that plaintiffs did not have the resources to repay defendants. This Court, rather than declaring a general rule that all class action determinations were subject to immediate review by the Courts of Appeals, specifically stated that it was the District Court's Order in that case imposing 90% of the notice costs on respondents that fell within "that small class" of decisions reviewable under the *Cohen* directive. 417 U.S. at 172. The Court said that the order on notice:

> ". . . *conclusively* rejected respondents' contention that they could not lawfully be required to bear the

[13] *Eisen* v. *Carlisle & Jacquelin,* 417 U.S. 156 (1974).

> expense of notice to the members of petitioner's proposed class. Moreover, it involved a collateral matter unrelated to the merits of petitioner's claims. Like the order in *Cohen,* the District Court's judgment *on the allocation of notice costs* was a final disposition of a claimed right which is not an ingredient of the cause of action and does not require consideration with it, id., at 546-547, 69 S.Ct. at 1226, and it was similarly appealable as a final decision under § 1291. In our view the Court of Appeals therefore had jurisdiction to review fully the District Court's resolution *of the class action notice problems* in this case . . ." (emphasis added) 417 U.S. at 172.

None of the extraordinary and final determinations in the *Eisen* case is present in the instant class action certification appealed from. Rather, the instant interlocutory class certification order is similar to all the other orders which have been held to be "non-final" and which determinations this Court has previously declined to review on many occasions subsequent to the *Eisen IV* decision. See, *Touche Ross & Co.* v. *Fabrikant,* 96 S.Ct. 424 (1975); *Touche Ross & Co.* v. *Seiffer,* 96 S.Ct. 779 (1976); *Cessna Aircraft* v. *White,* 96 S.Ct. 363 (1975).

Petitioner argues that respondents are not proper class representatives and that the District Court was wrong in not disqualifying them. This is clearly an issue that does not fall within the *Cohen* doctrine. *In re Cessna Air. Distrib. Antitrust Litigation, supra; Rodgers* v. *United States Steel Corp.,* 508 F.2d 152 (3rd Cir. 1975), *cert. denied,* 96 S.Ct. 54. It is neither a final disposition of the entire case, nor a final disposition of that issue.

Petitioner argues that the Third Circuit erred in not applying to this interlocutory class action determination

a review similar to that enunciated by the Court of Appeals for the Second Circuit.[14] However, in *Parkinson* v. *April Industries, Inc.*, 520 F.2d 650, 658 (2d Cir. 1975), the Second Circuit clearly holds that no appeal lies from a

> "discretionary ruling of the district judge that the prerequisites of Rule 23(a) and the requirements of Rule 23(b)(3) have been satisfied."

The District Court's decision in the case at bar was precisely such a "discretionary ruling." Accordingly, the dismissal of the appeal from that decision is in full agreement with the rule of the Second Circuit and of every other circuit court of appeals.[15]

In sum, the petition presents no question warranting review by this Court. The Court of Appeals was eminently correct in ruling that petitioner cannot appeal as a matter of right from the exercise of the trial judge's discretion in entering an interlocutory order certifying this suit as a class action under Rule 23, and there exists no conflict between the decision below and any decision of this Court or of any Circuit Court.

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[14] But see, *In re Master Key Antitrust Litigation*, 528 F.2d 5 (2d Cir. 1975), where the Court, rather wistfully, notes that other circuit courts have held that class action certification orders are not appealable as final orders, but that the pr edents in its circuit required it, however, to apply a three-pronged test which might permit appeal from such orders in an extremely narrow range of circumstances.

[15] See the cases cited on p. 9 herein.

POINT II

Petitioner's Attempt to Have This Court Make a Factual Determination That Respondents Acted Unethically, a Determination That Would Be At Odds With the Prior Decisions of the District Court and the Court of Appeals, Is Clearly Improper.

Contrary to petitioner's assertions, the decision of the Court below does *not* raise important issues with respect to the application of law. Petitioner is vainly seeking another hearing on its charges that respondents are unethical, that they have committed professional improprieties and deceit, and the like. These charges have not been sustained either in the District Court or the Court of Appeals, as petitioner itself recognizes. See Petition For Writ of Certiorari, p. 31.

It is clear that petitioner is misusing this Court's certiorari jurisdiction in its attempt to obtain a factual determination more in accordance with its perception of respondents. Chief Justice Taft, commenting on the Supreme Court's certiorari jurisdiction said:

> "The jurisdiction was not conferred upon this Court merely to give the defeated party in the Circuit Court of Appeals another hearing". *Magnum Import Co.* v. *Coty*, 262 U.S. 159, 163 (1923).

Petitioner's reliance on *Kriger* v. *European Health Spa, Inc. of Milwaukee, Wis.*, 56 F.R.D. 104 (E.D.Wis. 1972); *Shields* v. *First National Bank of Arizona*, 56 F.R.D. 442 (D. Ariz. 1971); *Cotchett* v. *Avis Rent A Car System, Inc.*, 56 F.R.D. 549 (S.D.N.Y. 1972), and *Graybeal* v. *American Savings & Loan Association*, 59 F.R.D. 7 (D.D.C. 1973) [all cited on p. 26 of the Petition For Writ of Certiorari] is entirely misplaced. In these cases, the District

Court determined that, for a variety of reasons, the requirements of Rule 23 had not been satisfied and therefore denied class determination. For example, in *Cotchett,* the trial judge determined that plaintiff failed to demonstrate that issues common to the class predominate over individual questions or that the class action device was superior to other available methods of adjudication. In *Kriger* and in *Shields,* the trial judge determined that plaintiff failed to show that the class action was superior to other available methods of adjudication. In *Graybeal,* the plaintiff failed to establish that: common issues predominated over individual questions, a class action would be superior to other methods of adjudication, or that he was an adequate class representative.

Moreover, none of these cases support the petitioner's arguments that an immediate appeal as a matter of right lies from an interlocutory order of the District Court, in which as a matter of discretion, the trial judge finds that the requirements of Rule 23 had been met.

Finally, petitioner argues that it faces irreparable harm if it is not permitted to immediately appeal the class certification order determining that respondents are adequate class representatives because if respondents lose at trial other class members may challenge the res judicata effect of the judgment against them. This argument ignores that class members may freely choose whether or not to stay in the class and be bound by any judgment pro or con. But more importantly, this argument can be made with respect to *every* decision certifying a class under Rule 23 because in every such instance, the trial court is making a determination of the adequacy of representation of the class representatives, in many cases over the objections of the defendants. As we have seen all the Courts of Appeals have held that such discretionary and non-final Rule 23

determinations by the trial judge are reviewable only after final judgment. Further, the *Gonzales* decision,[16] cited by petitioner at p. 32 of its petition for writ of certiorari, rather than supporting petitioner's arguments for the right to immediate appeals from Rule 23 determinations, supports the proposition that appellate review of the adequacy of the class representation should not be made until after the conclusion of the suit. In *Gonzales,* the Court stated that:

> "We hold that the primary criterion for determining whether the class representative has adequately represented his class for purposes of res judicata is whether the representative, through qualified counsel, vigorously and tenaciously protected the interests of the class. A court must view the representative's conduct of the *entire* litigation with this criterion as its guidepost." 474 F.2d at 75 (emphasis added)

In sum, petitioner has asserted no valid ground for departing from the final judgment role and permitting an immediate appeal from the interlocutory order below certifying this as a class action, and petitioner's attempt to have this Court make a factual determination that respondents have acted with impropriety, a determination contrary to the previous determinations of the District Court and the Court of Appeals, is a misuse of this Court's certiorari jurisdiction.

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[16] *Gonzales* v. *Cassidy,* 474 F.2d 67 (5th Cir. 1973).

The petition presents no question warranting review by this Court and should be denied.

Dated: New York, New York
July 6, 1976

Respectfully submitted,

DONALD N. RUBY
845 Third Avenue
New York, New York 10022
Attorney for Respondents

LESTER L. LEVY
WOLF POPPER ROSS WOLF & JONES
845 Third Avenue
New York, New York 10022
Of Counsel

APPENDIX

(a) 28 U.S.C. § 1291 provides:

"FINAL DECISIONS OF DISTRICT COURTS—The courts of appeals shall have jurisdiction of appeals from all final decisions of the district courts of the United States, the United States District Court for the District of the Canal Zone, the District Court of Guam, and the District Court of the Virgin Islands, except where a direct review may be had in the Supreme Court."

(b) 28 U.S.C. § 1292(b) provides in relevant part:

"INTERLOCUTORY DECISIONS . . .

(a) . . .

(b) When a district judge, in making in a civil action an order not otherwise appealable under this section, shall be of the opinion that such order involves a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation, he shall so state in writing in such order. The Court of Appeals may thereupon, in its discretion, permit an appeal to be taken from such order, if application is made to it within ten days after the entry of the order . . .".

(c) F.R. Civ. P. 23 provides, in relevant part:

"RULE 23. CLASS ACTIONS—(a) Prerequisites to a Class Action. One or more members of a class may sue or be sued as representative parties on behalf of

all only if (1) the class is so numerous that joinder of all members is impracticable, (2) there are questions of law or fact common to the class, (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and (c) the representative parties will fairly and adequately protect the interests of the class.

(b) Class Actions Maintainable. An action may be maintained as a class action if the prerequisites of subdivision (a) are satisfied, and in addition:

• • •

(3) the court finds that the question of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy. The matters pertinent to the findings include: (A) the interest of members of the class in individually controlling the prosecution or defense of separate actions; (B) the extent and nature of any litigation concerning the controversy already commenced by or against members of the class; (C) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; (D) the difficulties likely to be encountered in the management of a class action.

(c) Determination by Order Whether Class Action to be Maintained; Notice; Judgment; Actions Conducted Partially as Class Actions.

(1) As soon as practicable after the commencement of an action brought as a class action, the court shall determine by order whether it is to be so maintained. An order under this subdivision may be conditional, and may be altered or amended before the decision on the merits."